In the Supreme Court
OF THE
United States

OCTOBER TERM, 1943

No.

THE EMPORIUM CAPWELL COMPANY
(a corporation),
Petitioner,

vs.

CLIFFORD C. ANGLIM,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

THE TRANSFER WAS EXEMPT FROM TAX UNDER TREASURY REGULATONS 71, ARTICLE 35(r).

The question is whether the transfer sought to be taxed occurred "wholly by operation of law" within the meaning of Article 35(r), and was therefore exempt from tax.

The Circuit Court of Appeals answered this question in the negative.[1] The decision of this Court in the *Seattle First National Bank* case answers it in the affirmative.

The opinion of Mr. Justice Murphy (to which there was no dissent) in the *Seattle* case, after pointing out the validity of the exemptions declared in the regulations, says:

> "It is clear that the consolidation or merger of the national bank and the state bank occurred through the voluntary acts of the respective directors and stockholders pursuant to the provisions of Section 3 of the National Banking Act, with the approval of the Comptroller of the Currency. If the words 'wholly by operation of law,' as used in the administrative regulations, refer here to the entire process of consolidation, of which the transfer of securities is an essential part, the exemption cannot be applied. But in a broad sense, few if any transfers ever take place 'wholly by operation of law' for every transfer must necessarily be a part of a chain of human events, rarely if ever other than voluntary in character. Thus to give any real substance to the exemption, we must take a more narrow view and examine the transfer apart from its general background. We must look only to the immediate mechanism by which the transfer is made effective. If that mechanism is entirely statutory, effecting an automatic transfer without any voluntary action by the parties, then the transfer may truly be said to be 'wholly by operation of law.'

[1] Its opinion declares (R. 111): "Here, there was co-operation and participation of the stockholders, board of directors and the two corporations. The assets in this case could only be transferred to the stockholders in Delaware by the act of the parties."

> Here the actual transfer to respondent of the legal and beneficial title to the securities owned by the state bank was not effected by or dependent on any of the voluntary acts relating to the consolidation agreement or the ratification or approval thereof. * * * Rather the transfer occurred solely and automatically by virtue of Section 3 of the National Banking Act."

By the same process of reasoning, the transfer in the case at bar occurred "solely and automatically" by virtue of the statutory provisions of California and Delaware authorizing the merger. Under these statutes, the procedure resulting in the merger was initiated by the agreement of the two corporations, just as, under Section 3 of the National Banking Act,[2] the first step toward the consolidation considered in the *Seattle First National Bank* case consisted of the making of an agreement of consolidation by the directors of the two banks involved. Under either the National Banking Act or the merger statutes of California and Delaware, the terms and conditions of the merger are set forth in the agreement. To ascertain what those conditions are one must look to the agreement, but, as held in the *Seattle First National Bank* case, those terms and conditions become effective and operative by reason of the statute which permits the merger or consolidation.

Thus, applying the language of this Court in the Seattle case, it is the merger statute (or statutes) "that is the mechanism by which the transfer of securities is made effective. No voluntary act of the parties is neces-

[2] 12 U.S.C., sec. 34a.

sary." Under Section 361(5) of the Civil Code of California, the agreement becomes effective only when, with the necessary certificates, it is filed with the Secretary of State, and thereupon "the several parties thereto shall be one corporation". Under the Delaware Corporation Law (Sec. 59), the agreement, certified and acknowledged, shall be filed in the office of the Secretary of State "and shall thence be taken and deemed to be the agreement and act of consolidation or merger of said corporations".

The transfer here involved was a transfer of common stock of the California corporation, theretofore owned by the Delaware corporation, to the stockholders of the latter, which expired through the merger and whose own shares were extinguished thereby. The transfer was specifically provided for by the agreement of merger, which declared (R. 12) that "such merger shall effect the transfer, from The Emporium Capwell Corporation to the holders of the said 412,853 shares of its capital stock proportionately, of all the issued and outstanding common stock of The Emporium Capwell Company, being 412,853 shares without par value, all presently held by The Emporium Capwell Corporation".

This provision for the transfer of the stock of the California corporation, theretofore held by the Delaware corporation, was properly included in the agreement of merger (and hence in the legal effect of the merger itself) by both the California and the Delaware statutes. Section 361(1) of the Civil Code of California provides that the agreement between the two corporations shall set forth "the terms and conditions of merger or con-

solidation, and the mode of carrying the same into effect, *as well as the manner and basis of converting the shares of the constituent corporations into the shares of the consolidated or surviving corporation*". (Emphasis supplied.) The same provision, in almost identical words, is contained in the Delaware statute (Sec. 59).

It is submitted therefore, that the transfer did not, and could not, become effective except through the merger, which itself was made effective and operative by virtue of the statutes of the two states. It was the statutes alone which gave operative effect to all the provisions of the agreement, including the provision that "such merger shall effect the transfer".[3]

II.

THE TRANSFER WAS ALSO EXEMPT FROM TAX UNDER TREASURY REGULATIONS 71, ARTICLE 35(e).

At the time of the merger, Regulations 71, Article 35(e), read as follows:

---

[3]No legal significance attaches to the fact included in the "Stipulation as to Certain Facts" (R. 71-72) that the certificate for shares of the common stock of the California corporation owned by the Delaware corporation was endorsed by the latter and delivered to the Transfer Agent of the former. The same Stipulation includes the letter of the California corporation accompanying the delivery (R. 75) and showing that the certificate was delivered after the merger had become effective, that the California corporation maintained that the stock had already been transferred "pursuant to the agreement of merger", and that the certificate was delivered for purposes "of record on the books of this company". The surrender of the endorsed certificate did not transfer title, since, as the California corporation correctly stated, the transfer had already taken place by virtue of the merger. (*Mastin v. Mastin*, 99 Fed. 435.)

"Article 35. Sales or transfers not subject to tax. The following are examples of transactions not subject to the tax:

(e) The transfer of the stock of a merged corporation in exchange for stock of the merging corporation at the time and as part of a statutory merger, and the substitution of new certificates for the certificates representing the old stock of the merging corporation."

To interpret and apply the Regulation, it is necessary to first answer this question:

Which of the two corporations, parties to a merger, is referred to by the Regulation as the "merged" corporation and which as the "merging"?

We contend that the surviving corporation (California) is the one designated as "merged", and the dying or absorbed corporation (Delaware) is the one designated as "merging".

Obviously, if this view be correct, the transfer here sought to be taxed falls directly within the terms of subdivision (e). It was a transfer of stock of the California corporation at the time and as part of a statutory merger. It was a transfer in exchange for stock of the Delaware corporation, as shown by paragraphs (4a) and (5a) of the merger agreement (R. 12-13; 13-15), defining the terms and conditions of the merger and the manner and basis of converting the shares. It also, clearly, involved the substitution of new certificates (of the California corporation) for the certificates representing the old stock of the merging (Delaware) corporation.

In rejecting the petitioner's claim of exemption under Article 35(e), the Circuit Court of Appeals based its reasoning (R. 105-106) upon the assumption that the Regulation designates the surviving (California) corporation as the "merging" corporation and the defunct (Delaware) corporation as the "merged" corporation. It is respectfully urged that this interpretation directly transposes the true meaning of the words "merging" and "merged", as used in the Regulation.

We submit, briefly, the reasons which we believe should lead to the conclusion that subdivision (e) must be read as meaning, by "merged" corporation, the continuing one, and by "merging", the dying one:

(a) The contrary interpretation—the one adopted by the Circuit Court of Appeals—would make the Regulation meaningless and ineffective for, if "merged" corporation means the one that goes out of existence, and "merging" the one that survives, it is difficult or impossible to imagine a situation to which the exemption declared by subdivision (e) could apply. The last clause of the subdivision contemplates the issuance of new certificates and the substitution of them for certificates representing the old stock of the "merging" corporation. If new certificates are substituted for old, clearly the new certificates are those of the surviving corporation, and certificates representing "old stock" are certificates of stock of the absorbed or dying corporation. The term "new certificates" must refer to certificates of stock which is to have a continuing existence and validity. It cannot apply to certificates of stock in a corporation

which expires in the merger and whose stock ceases to exist after the merger. Likewise, if certificates are substituted for certificates representing "old stock", the substitution contemplated can only be of something having continuing validity for something which has ceased to have value or life. The "new" is clearly a stock which is to endure, the "old" a stock which is wiped out.

(b) Our position is fortified by a consideration of subdivision (d) of Regulations 71, Article 35, in effect at the time of this merger (see Appendix). That subdivision dealt with consolidations. As applied to corporations, consolidation and merger are closely parallel. In each, two or more corporations unite.

Subdivision (d) included in transfers exempt from tax "the surrender of the stock of the consolidating corporation in exchange for stock of the consolidated corporation". Comparing this subdivision with (e), we have two provisions which apply to similar situations, and should therefore be given like construction in so far as they contain the same word or words of the same grammatical form. It is not to be supposed that the Treasury Department, in framing these Regulations, distinguished between the continuing corporation and the extinguished corporation by designating the former as "consolidated" and the latter as "consolidating" in subdivision (d), and used the parallel terms "merged" and "merging" in the opposite sense in subdivision (e). It is submitted that whichever of the corporations is meant by "consolidating" in (d) is the one meant by "merging" in (e), and that the one designated as "consolidated" in

(d) is the one designated as "merged" in (e). It can hardly be doubted that under (d) the corporation which is to have a continuing future existence is the "consolidated" corporation. Not only is this the meaning apparent on the face of the words used, but it is, for reasons indicated above with respect to subdivision (e), the only one which would give the exemption any purpose or effect.

(c) Amendments of the Regulations adopted in 1942 throw light on the meaning of the former subdivision (e) and indicate clearly that the term "merged" in the former (and here applicable) regulation refers to the surviving entity (California) and that the "merging" corporation refers to the extinguished (Delaware) corporation. In the revised and now current form of regulations, the examples of transfers not subject to tax are found in Section 113.34 of Regulations 71. Both (d) and (e) in their earlier form are dropped from the revision. An example of a sale or transfer not subject to tax, as it has to do with a merger, now appears as subdivision (i) of Section 113.34. It reads as follows:

> "In a merger of corporations the surrender of stock of both the merging and continuing corporations in exchange for stock of the continuing corporation."

Without considering any change in substantial effect that may have been worked by this revision (which is not applicable in the instant case[4]), the verbiage is significant as indicating the meaning of the words "merging" and "merged" in the former subdivision (e). The

---

[4] *Helvering v. Reynolds Tobacco Co.*, 306 U.S. 110, 115.

new subdivision (i) retains the word "merging". It uses the word in contradistinction, not to "merged", but to "continuing". Presumably, the word "merging", which appears in both the old (e) and the new (i), has the same meaning in both. In each of the regulations it describes one of the two corporations which are parties to a merger. The other party, then, is clearly the "merged" corporation designated in (e), or the "continuing" corporation designated in (i). Under the new provision there can be no question as to which corporation is meant by each phrase. The "continuing" corporation is clearly the one which survives. The other, the "merging" corporation, must therefore be the expiring one. Where the same word ("merging") appears in both the old and the amended regulations, it cannot fairly be thought that it was used in contradictory senses in the two regulations. By opposing to it in the new regulation the word "continuing", any possible doubt as to the meaning of "merging" is removed. It becomes clear that "merged", in the old subdivision (e), was used to designate the "continuing" or surviving corporation.

CONCLUSION.

It is submitted that the transfer should be held to be exempt from tax under each of the regulations relied upon by petitioner; that the writ of certiorari should be granted, the judgment of the Circuit Court of Appeals reversed, and that court directed to enter judgment reversing the judgment of the District Court and directing

said District Court to enter judgment in favor of your petitioner, as prayed in the complaint.

Dated, San Francisco, California,
April 19, 1944.

Respectfully submitted,
M. C. SLOSS,
E. D. TURNER, JR.,
Attorneys for Petitioner.

SLOSS & TURNER,
Of Counsel.

(Appendix Follows.)